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No.

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1987

THEODORE S. PROUD, JR.,

Petitioner,

v.

GREYCAS, INC., a corporation,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

1. Whether this Court's holding in *Nat'l Savings Bank v. Ward*, 100 U.S. 195 (1879) is viable and whether an attorney owes a duty to the adverse side of a business transaction, even though both parties were represented by their own attorneys, such that the attorney may be liable in negligence?

2. Whether the Seventh Circuit was required to apply the law of Illinois, as the forum state, in this diversity action under this Court's holding in *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1937)?

3. Whether the respondent proved all elements necessary to recover for a negligence action under Illinois law and whether petitioner proved his defense of comparative negligence?

4. Whether 28 U.S.C. § 1728 and the doctrine of collateral estoppel were properly applied where the petitioner was not a party and had no opportunity to litigate but the judgment of a prior state court action was admitted as proof of respondent's damages?

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The petitioner Theodore S. Proud, Jr. respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit, entered in the above entitled proceeding on August 3, 1987.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit is reported at 826 F. 2d 1560, and is reprinted in the appendix hereto, p. 1a, *infra*. The Seventh Circuit's order denying the petition for rehearing is reprinted in the appendix hereto, p. 17a, *infra*. The order and memorandum opinion of the United States District Court for the Southern District of Illinois (Beatty, D.J.) has not been reported. It is reprinted in the appendix hereto, p. 18a, *infra*.

JURISDICTION

Respondent filed this action in the United States District Court, Southern District of Illinois invoking diversity jurisdiction pursuant to 28 U.S.C. § 1332. After a non-jury trial, a final judgment was entered on July 15, 1986 (see pp. 18a-24a, *infra*). An appeal was brought by petitioner pursuant to 28 U.S.C. § 1291. The Seventh Circuit affirmed on August 3, 1987 (see p. 1a, *infra*) and denied the petition for rehearing on September 1, 1987 (see p. 17a, *infra*).

The jurisdiction of this Court to review the decision of the Seventh Circuit is invoked under 28 U.S.C. § 1254(1).

STATEMENT OF THE CASE

The respondent agreed to make a loan to a borrower, not party to this action, to be secured by farm equipment. Under the terms of the loan agreement, the borrower was required to retain an attorney and obtain his advice as to whether the provisions of the loan agreement were binding and enforceable on the borrower. Under the security documents, the borrower's attorney was also to sign a letter as to whether the borrower owned the property free of any encumbrances, and whether the lender's interest in the security was recorded. The petitioner in this case was the attorney retained by the borrower.

The respondent was also represented by its own attorney in this business transaction. The respondent is an international corporation in the business of making loans and had a credit committee with the ultimate authority to approve loan applications. To assist it in determining whether a loan should be made, it not only had in-house legal counsel, but various departments which conducted investigations on the borrower.

As to this transaction, as a result of the various investigations, the respondent had information before it which put it on notice that this loan should not be made. It knew that the borrower was "in a hurry" to borrow in excess of $1.3 million to pay off outstanding bills. It knew that the borrower's financial statements were unaudited, which was considered to be a "red flag" on any loan transaction. It was aware that the borrower had insufficient cash flow the prior year to service his present debts, totalling about $2.91 million. The respondent also knew that the proposed collateral equipment for this loan had been purchased in the last two and one-half years, and that during this same time period, there were ll financing statements filed against the borrower's farm equipment. It was told that the $1.3 million loan was to be secured with $865,000 of collateral equipment according to one appraisal. It also knew that the borrower's equipment was insured for $300,000, at a

time the borrower claimed it was worth $865,000, raising the obvious inference that the borrower did not have the equipment he claimed, or that others with an interest in the equipment were insuring it. The credit committe was advised by its appraisal department that there was a 35% risk exposure in that if the borrower defaulted on the loan, the respondent would probably lose 35% of its loan.

With this background of information, the credit committee tabled this transaction three times. The first time, it ordered its own attorneys to obtain a list of the collateral equipment which detailed the make, model, serial number and number of hours of use for each piece of equipment. It also told its attorney to obtain an explanation as to why two of the borrower's financial reports were inconsistent. The second time the transaction was tabled, the credit committee ordered its own attorney to conduct the title search on the proposed collateral. In the past, the respondent's own attorneys had conducted title searches, contrary to its usual practice of relying on the borrower's attorney. The last time the credit committee met to consider this loan, it again ordered its attorney to obtain a list detailing information on the equipment.

It was uncontested that it was the respondent's attorney's responsibility to fulfill all the conditions and requirements set by the credit committee or contained in the loan documents in any transaction. In this transaction, the respondent's attorney did not follow through on his client's specific directions. A list detailing the specifics on the equipment was never obtained, nor made part of the loan documents. The respondent's attorney never conducted the title search himself, instead unilaterally deciding to rely on the borrower's attorney's letter.

The respondent's attorneys never contacted the petitioner, the borrower's attorney, on whom they later claimed to rely. All information, including the letter on which this action is based, was delivered to or by the

borrower. The respondent's attorneys prepared all the documents in relation to this loan transaction, including the letter to be signed by the borrower's attorney and the U.C.C. financing statement, both with attached lists of equipment. Instead of sending the U.C.C. statement to the County Clerk's office for filing, or to the borrower's attorney who, according to the respondent's attorney, had the duty to see that it was filed, it was delivered to the borrower to deliver to his attorney. Likewise, the letter to be signed by the borrower's attorney was delivered to the borrower himself.

The letter stated that the petitioner was the attorney for the borrower, and that "[t]he loan agreement constitutes a valid obligation of the [borrower] binding and enforceable against the [borrower] in accordance with its terms." The letter also stated that he had conducted a U.C.C., tax and judgment search and that the equipment was free of liens or encumbrances. It did not say that the petitioner had filed the respondent's financing statement, but notes that it was filed on March 19, 1981. In fact, a financing statement, with a substituted list of collateral, had been filed by the borrower before the petitioner signed the letter. The petitioner, who had known the borrower, also an attorney and petitioner's brother-in-law, for 20 years, asked if all conditions had been met as stated in the letter and was told yes. In reliance of the borrower's assurances, the petitioner signed the letter.

In the fall of 1981, within 6 months of the loan closing, the borrower was in default. Five months later, he was found dead of asphyxiation in a barn, a presumed suicide.

Upon his death, various creditors, including the respondent, filed claims against the estate and instituted state court law suits claiming their loans had been secured by the same equipment as the respondent's. Two state court suits were consolidated, and the rights of the various creditors, party to the suits, had been determined by the

time this cause was tried. Respondent filed a counterclaim against the borrower's wife, who was a cosigner on the loan agreement and who had signed a personal guarantee on the loan. The respondent's claims against the estate in the probate court were still pending at the time of trial, and the respondent's claim against the borrower's wife had not been prosecuted.

There were also life insurance proceeds totalling $4.0 million. The borrower's wife received $2.5 million, to be held in two trusts. At least $250,000 plus accrued interest would be included in the estate under the trust terms if the estate's assets were insufficient to satisfy creditor's claims. The record was unclear if the borrower's wife would retain the other $2.0 million, or if this would also go to the estate. In addition, there were other insurance policies for $1.75 million. At the time of trial, the Internal Revenue Service had a pending claim against all insurance proceeds, claiming $1.5 million for federal estate tax. Although the administrator testified that the estate's present assets were insufficient to satisfy the respondent's claim, the record was devoid of evidence as to whether the $4.0 million, less tax, would be sufficient to pay the respondent's claim.

Pretrial Proceedings Before the District Court

The respondent filed this suit alleging the petitioner had been negligent in representing that he had conducted the title search, the equipment was free of encumbrances, and the respondent's security interest was perfected. It alleged that it relied on these representations in making the loan and that the borrower's estate and the borrower's wife, as cosigner, had insufficient assets to pay the outstanding loan. It further alleged that as a result of petitioner's failure "to act in a professional manner and in accordance with the standards of their[1] profession" it had been damaged.

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[1] This suit was brought against another attorney whose motion for directed verdict was granted. No appeal was sought by respondent as to this attorney.

Petitioner's motion to dismiss on the grounds that an attorney owes no duty to the other side of a business transaction was denied. The petitioner's defenses included the respondent's comparative negligence and respondents' failure to prosecute viable actions against the estate and the co-borrower, thus it could not show it had sustained any actual damages.

District Court's Decision and Judgment

After a bench trial, the court entered judgment for the respondent, finding that the petitioner had "failed to exercise the standard of care of a reasonably prudent attorney and was negligent in the giving of his opinion letter" in that he had not conducted the title search nor had he perfected the respondent's security interest, but instead relied on the borrower's representations that this had been done (see p. 19a, *infra*). The district court further found that there had been a financing statement filed, but a substituted list of equipment had been attached (see p. 20a, *infra*).

The district court found that the petitioner "may have proved negligence" on the respondent's part, but there was no causal relationship to the petitioner's malpractice or the damages (see p. 20a, *infra*). The district court did not rule on the issue of whether the respondent could recover against the petitioner when it still had pending claims against the co-borrowers. It found that, although petitioner was not a party to the state court actions, as a result of the prior adjudication in state court, the respondent lost any interest in the collateral equipment (see p. 20a, *infra*).

Opinion of the Seventh Circuit

The Seventh Circuit affirmed, analyzing the case as a legal malpractice claim and as a negligent misrepresentation claim (see p. 4a, *infra*). The Seventh Circuit held that the borrower's atttorney owed a duty to the lender, without addressing the fact that the lender was represented by its own attorney who had been instructed by his own client to conduct the title search (see pp. 5a-9a, *infra*). It found that the petitioner had not proven any comparative negligence on the part of the respondent, again not acknowledging that the respondent/lender was represented by its own attorneys, finding it had no obligation to perfect and protect its own security interest (see pp. 9a-11a, *infra*).

The Seventh Circuit held that the state court judgment was admissible to prove that the respondent had lost its interest in the collateral equipment (see p. 13a, *infra*). Once the judgment was admitted, the petitioner had the burden of proof to rebut the prior judicial determination as to the priority of the various creditor's claims (see pp. 12a-13a, *infra*).

The Seventh Circuit also did not directly address the issue of whether the respondent had shown any damages where it had pending claims against the estate and the co-borrower. Instead, it simply noted that if there were "hopes of recovering" there "would be a serious question whether it had actually sustained the full damages" sought in this case (see p. 15a, *infra*). It then resolved this issue by stating the district court did not commit clear error in finding for the respondent on this question (see p. 15a, *infra*).

REASONS FOR GRANTING THE WRIT

I.

THIS COURT SHOULD EXERCISE ITS SUPERVISORY AUTHORITY TO DETERMINE THE IMPORTANT QUESTION OF WHEN A NON-CLIENT MAY MAINTAIN SUIT AGAINST THE ATTORNEY FOR HIS OPPONENT

This case raises the important question of under what circumstances, if any, may a non-client maintain an action against his opponent's attorney. In this case, the respondent/lender, who was represented by its own attorneys in this business transaction, sued the attorney for the borrower. This case presents two issues of importance which should be determined by this Court in the exercise of its supervisory authority. First, must there be privity of contract in order to maintain a suit against an attorney, as this Court held in *Nat'l Savings Bank v. Ward*, 100 U.S. 195 (1879). Second, whether a duty is owed to an adverse party, despite a conflict of interest for the attorney.

In *Nat'l Savings Bank v. Ward*, 100 U.S. 195 (1879), this Court held that a non-client could not recover from an attorney who represented the other side of the business transaction in the absence of privity. Since *Ward*, a number of state courts have held that in the absence of privity, a non-client has no right of action against an attorney for negligence. *See, Page v. Frazier*, 388 Mass. 55, 445 N.E.2d 148 (1983); *Bell v. Manning*, 613 S.W.2d 335 (Tex.App.Ct. 1981); *Ames Bank v. Hahn*, 205 Neb. 353, 287 N.W.2d 687 (1980); *Amey, Inc. v. Henderson, Franklin, Starnes & Holt, P.A.*, 367 So.2d 633 (Fla.App.Ct.), *cert. denied*, 376 So.2d 68 (1979); *Chalpin v. Brennan*, 114 Ariz. 124, 559 P.2d 680 (Ariz.App.Ct. 1976), *but see, Donnelly Constr. Co. v. Oberg/Hunt/Gilleland*, 139 Ariz. 184, 677 P.2d 1292 (1984); *see also, Flaherty v. Weinberg*, 303 Md. 115, 492 A.2d 618, 620, n.2 (1985) and the citations therein.

Other jurisdictions, however, have refused to follow the holding in *Nat'l Savings Bank v. Ward*, holding that privity of contract is not a prerequisite for a non-client to maintain an action against an attorney, primarily utilizing two analyses. The first is a balancing of factors test as first applied by the California Supreme Court in *Lucas v. Hamm*, 56 Cal.2d 583, 15 Cal.Rptr. 821, 364 P.2d 685 (1961), *cert. denied*, 368 U.S. 987 (1962); *Flaherty*, 493 A.2d at 621-22. The other test is based on a third party beneficiary theory, under which a non-client may sue the attorney if he can prove that the primary intent of the attorney/client relationship was to directly benefit the plaintiff. *Flaherty v. Weinberg*, 303 Md. 113, 492 A.2d 618 (1985); *Guy v. Liederbach*, 501 Pa. 47, 459 A.2d 744 (1983); *Pelham v. Greisheimer*, 92 Ill.2d 13, 440 N.E.2d 96 (1982). Such a situation typically arises where the beneficiary of a will sues the attorney who negligently drafted it. *See, e.g., Ogle v. Fuiten*, 102 Ill.2d 356, 466 N.E.2d 224 (1984).

The determination of whether a duty is owed to an adverse party necessarily involves the consideration that there is a potential conflict of interest. An attorney owes the duty of undivided loyalty to his client. Many courts have refused to find that an attorney owes a duty to the adverse party in a business transaction as a matter of public policy because such a situation would create a conflict of interest. *Flaherty*, 492 A.2d at 626, 629; *Bell*, 613 S.W.2d at 338; *Page*, 445 N.E.2d at 153; *Amey, Inc.*, 367 So.2d at 635; *Chalpin*, 559 P.2d at 681; *Adams v. Chenowith*, 349 So.2d 230, 231 (Fla.App.Ct. 1977). As one court noted, in holding there was no duty owed to a non-client:

> The attorney's preoccupation or concern with the possibility of claims based on mere negligence (as distinguished from fraud) by any with whom his client might deal would prevent him from devoting his entire energies to his client's interest. The result would be both an undue burden on the profession and a dimunition in the quality of the legal services received by the client.

Bell 613 S.W.2d at 339. Other courts have refused to extend the duty of an attorney to a non-client on the grounds that it would encourage parties to forego legal representation and, if dissatisfied, look to the opponent's attorney for recovery. *Bell*, 613 S.W.2d at 339; *Chalpin*, 559 P.2d at 681.

Not all courts recognize this policy consideration and have found that an attorney owes a duty to the adverse party without addressing the conflict of interest question. *United Leasing Corp. v. Miller*, 45 N.C.App. 400, 263 S.E.2d 313, *appeal denied*, 300 N.C. 374, 267 S.E.2d 685 (1980); *Bradford Sec. Processing Serv., Inc. v. Plaza Bank & Trust*, 653 P.2d 188 (Okla. 1982); *Roberts v. Ball, Hunt, Hart, Brown & Baerwitz*, 57 Cal.App.3d 104, 128 Cal.Rptr. 901 (1976). In this case, the court found that such a duty was owed, ignoring the fact that the respondent/lender was represented by its own attorney in this loan transaction. Neither the district court nor the court of appeals ever addressed the question of whether the respondent could maintain this action against its opponent's attorney even though the situation was adversarial.

Because this Court's holding in *Nat'l Savings Bank v. Ward* is not being followed by state courts, this Court should accept this petition to determine whether its holding is still viable. This case also involves the important question of under which circumstances may a non-client sue his opponent's attorney. A finding that an attorney owes a duty to a party whose interests are adverse to the client's involves important principles as to the scope and extent of an attorney's duty, including an attorney's duty of undivided loyalty owed to his client and the prohibition against simultaneously representing adverse parties. The decision in this case allowing the respondent to maintain a suit for negligence against the opponent's attorney, when it had the representation of its own attorney, is an erosion of important legal principles. For these reasons, petitioner

requests this Court to accept this petition and give this case its plenary consideration.

II.

THE COURT OF APPEALS VIOLATED THIS COURT'S DECISIONS REQUIRING FEDERAL COURTS TO APPLY STATE LAW IN DIVERSITY CASES

In *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938), this Court held that in diversity actions, federal courts had to apply the law of the forum state. Because Illinois law was not followed, this Court's holding in *Erie* was disregarded and this case was decided in a way contrary to the usual course of judicial proceedings.

Under Illinois law, in order to recover from another for negligent misrepresentation, a plaintiff must plead and prove that the defendant owed a duty, there was a breach thereof, damages proximately resulted, and the plaintiff justifiably relied on the representations. *Duhl v. Nash Realty, Inc.*, 102 Ill.App.3d 483, 493-94, 429 N.E.2d 1267, 1276 (1981); *Luciani v. Bestor*, 106 Ill.App.3d 878, 888, 436 N.E.2d 251, 259 (1981). The Seventh Circuit did not follow Illinois law as to three of these essential elements: duty, justifiable reliance, and damages.

A. Attorneys Owe No Duty to a Non-Client Where the Matter Is Adversarial and There Is a Potential Conflict.

The general rule in Illinois is that an attorney owes no duty to a non-client where the matter could create a conflict of interest or is adversarial. *Pelham v. Griesheimer*, 92 Ill.2d 13, 23-24, 440 N.E.2d 96, 100 (1982); *Makela v. Roach*, 142 Ill.App.3d 827, 830, 492 N.E.2d 191, 193-94 (1986); *Doyle v. Shlensky*, 120 Ill.App.3d 807, 812, 458 N.E.2d 1120, 1125, 1126 (1983). The public policy underlying this rule is to prevent the conflict of interest that is inherent whenever an attorney owes duties simultaneously to both sides. *Pelham*, 92 Ill.2d at 23-24, 440 N.E.2d

at 100-01; *Schott v. Glover*, 109 Ill.App.3d 230, 234-35, 440 N.E.2d 376, 379 (1982).

Illinois courts will recognize that an attorney may owe a duty to a non-client only in the most limited circumstances. The sole factual situation where Illinois courts have found such a duty is where the relationship was non-adversarial: the attorney was retained to draft a will and the plaintiffs alleged they were the intended beneficiaries. *Ogle v. Fuiten*, 102 Ill.2d 356, 363, 466 N.E.2d 224, 227 (1984).

The factors which Illinois courts apply in determining if a duty is owed are: 1) whether an attorney could have represented the other side's interest, regardless of whether an attorney was actually retained; 2) whether the matter was adversarial, i.e., whether there was a potential conflict; 3) whether the client's intent and the primary or direct purpose of the relationship was to confer a benefit on the non-client; and 4) whether the attorney had undertaken the performance of a task and, if so, whether the plaintiff could "justifiably rely" on the attorney's performance of that task. *Pelham*, 92 Ill.2d at 20-24, 440 N.E.2d at 100-01.

The Seventh Circuit clearly did not follow Illinois law in finding that a duty was owed to the non-client in this business transaction.[2] The primary fact which the Seventh

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[2] The Seventh Circuit stated that there was doubt as to whether this suit was brought for legal malpractice or negligent misrepresentation (see, pp. 4a, 6a, *infra*). However the complaint clearly alleges that the petitioner's failure "to act in a professional manner and in accordance with the standards of [his] profession" resulted in damages. The claimed failure to act professionally was the representations made in the letter. Further, the complaint alleges that the borrower retained the petitioner as his attorney "for the direct benefit of" the respondent. Thus this suit was brought for legal malpractice under a third party beneficiary theory.

(Footnote continued on the following page)

Circuit and the district court disregarded was that the respondent was represented at all times by its own attorney. Not only was the respondent represented by its own attorney, but the respondent had specifically ordered its own attorney to conduct the task which is the basis of this action, a title search, for which the respondent's attorneys decided to rely on the borrower's attorney.

Nor was the second consideration, that the interest not be adverse and there is no potential for a conflict, met in this case. In a business transaction, Illinois considers parties to a business transaction to be in an adversarial position. *Gold v. Vasileff*, 160 Ill.App.3d 125, 127-28, 513 N.E.2d 446, 448 (1987); *Torres v. Divis*, 144 Ill.App.3d 958, 964, 494 N.E.2d 1227, 1231 (1986); *see also, Practical Offset, Inc. v. Davis*, 83 Ill.App.3d 566, 574, 404 N.E.2d 516, 523 (1980) and *Bloomer Amusement Co. v. Eskenazi*, 75 Ill.App.3d. 117, 120, 394 N.E.2d 16, 18 (1979).[3] Conflicts

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2 *(Continued)*
Assuming this was a negligent misrepresentation claim, respondent would have had to plead and prove that the petitioner was in the business of supplying information to another for his guidance in business transactions with third parties. *Black, Johnson & Simmons Ins. Brokerage, Inc. v. IBM*, 109 Ill.App.3d 132, 134-135 440 N.E.2d 282, 284 (1982). Attorneys are not engaged in business, but are engaged in the practice of law. *C.f., Frahm v. Urkovich*, 113 Ill.App.3d 580, 447 N.E.2d 1007, 1010 (1983). In this case, the respondent expected the petitioner to practice law and represent that the provisions of the loan agreement were binding and enforceable on his client while at the same time place him in a position where he was in the business of supplying information to respondent for its guidance in the business transaction with the petitioner's own client. This created an inherent conflict.

[3] *Bloomer* was decided before the Illinois Supreme Court abolished the privity requirement in legal malpractice cases in *Pelham*, and is cited in *Pelham* for the proposition that an attorney is only liable to his client, with whom there is privity. The Illinois Supreme Court did not expressly overrule *Bloomer*, noting that it arose out of "substantially different factual situations." *Pelham*, 92 Ill.2d at 20, 440 N.E.2d at 99. In *Bloomer*,

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of interest may arise, for example, in contractual provisions as to prepayment or late charges, disclosure rights, or ramifications of guarantees. *See, Page v. Frazier*, 388 Mass. 55, 445 N.E.2d 148, 153 (1983).

In this case, the opinion letter specifically stated that the petitioner had been retained as the borrower's attorney and that he had read the loan documents and advised him that the provisions were binding and enforceable on his client. It was to the respondent's advantage to require the borrower to retain the petitioner as his independent attorney since under Illinois law the provisions of a contract are construed against the drafter, and the respondent was in a better position to defend against future attacks on the contract. *Dr. Charles W. Smith III, Ltd. v. Connecticut Gen. Life Ins. Co.*, 122 Ill.App.3d 725, 728, 462 N.E.2d 604, 606 (1984).

The Seventh Circuit did not follow Illinois law as to the third factor in determining whether or not an attorney owes a duty to a non-client. The Seventh Circuit stated that the test was whether "the primary purpose and intent of the attorney-client relationship itself was to *benefit or influence* the third party" citing to *Pelham v. Griesheimer*, 92 Ill.2d at 21, 440 N.E.2d at 100 (emphasis added) (see, p. 5a, *infra*). However, that is not the test where, as here, the interests are adversarial. The Illinois Supreme Court in *Pelham* specifically held that:

> In cases of an adversarial nature, in order to create a duty on the party of an attorney to one other than a client, there must be a clear indication that the representation of the attorney is intended to directly confer a benefit upon the third-party.

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3 *(Continued)*

as in this case, both parties were represented by their own attorneys. 75 Ill.App.3d at 120, 394 N.E.2d at 18. The court held that the plaintiff could not sue the opponent's attorney for negligence in conducting a title search. 75 Ill.App.3d at 119, 394 N.E.2d at 17.

92 Ill.2d at 23, 440 N.E.2d at 100. Thus, the Seventh Circuit's analysis with regard to "intent to influence" is not the standard by which a duty is found under Illinois law.

In this case, the respondent was at most an incidental beneficiary. The letter identified petitioner as the borrower's attorney and also stated that the loan agreement was binding and enforceable on the borrower. Any reliance that the respondent's attorneys placed on this letter was a calculated risk particularly where there had been no direct contact with the petitioner. Nor did the respondent prove the fourth factor, that of justifiable reliance, used in determining whether a duty is owed.

B. Respondent Had the Burden to Plead and Prove That It Justifiably Relied on the Opponent's Attorney.

The question of justifiable reliance is not only one factor in making the determination of whether an attorney owes a duty to a non-client (*Pelham*, 92 Ill.2d at 24, 440 N.E.2d at 101), but is also an indispensable element to proving an action for negligent misrepresentation. *Central States Joint Bd. v. Continental Assur. Co.*, 117 Ill.App.3d 600, 604, 453 N.E.2d 932, 935 (1983) *Luciani v. Bestor*, 106 Ill.App.3d 878, 888, 436 N.E.2d 251, 259 (1982)). Both the district and appellate courts, in considering the question of justifiable reliance, ignored the vital fact that the respondent was represented by its own attorney in this business transaction. By side stepping this undisputed fact, the court was able to ignore Illinois law which is clear that if a party has the advice of his own consultant or specialist, then any reliance on misrepresentations is unreasonable as a matter of law and recovery is barred. *Costello v. Liberty Mut. Ins. Co.*, 38 Ill.App.3d 503, 507-08, 348 N.E.2d 254, 258 (1976); *Central States*, 117 Ill.App.3d at 604, 453 N.E.2d at 935. This principle is equally applicable to actions against attorneys. *Thrall Car Mfg. Co.*

v. Lindquist, 145 Ill.App.3d 712, 495 N.E.2d 1132 (1986); *Bloomer Amusement Co. v. Eskenazi*, 75 Ill.App.3d 117, 120, 394 N.E.2d 16, 18 (1979); *Costello*, 38 Ill.App.3d at 507-08, 348 N.E.2d at 258.

Before a plaintiff can recover, he must prove not just that he relied, but that he had a "right to rely" on the representations. *Soules v. G.M.C.*, 79 Ill.2d 282, 286, 402 N.E.2d 599, 601 (1980). Under Illinois law, a plaintiff has an affirmative duty to use ordinary prudence in making an inquiry as to the truth of the representations before he can recover from the defendant. *Soules*, 79 Ill.2d at 286, 402 N.E.2d at 601; *Smith v. Ethell*, 144 Ill.App.3d 171, 174, 494 N.E.2d 864, 866 (1986); *Central States*, 117 Ill.App.3d at 605, 453 N.E.2d at 936.

The right to rely is measured not only by the actual knowledge a plaintiff had at the time, but also by all facts "of which he might have availed himself by the exercise of ordinary prudence." *Soules*, 79 Ill.2d at 286, 402 N.E.2d at 601. The law presumes that a plaintiff knows that which he would have known had he inquired. *Soules*, 79 Ill.2d at 286, 402 N.E.2d at 601; *Central States*, 117 Ill.App.3d at 607, 453 N.E.2d at 936. Only where parties do not have equal knowledge or means of obtaining knowledge is a party's reliance justified. *Central States*, 117 Ill.App.3d at 606, 453 N.E.2d at 936. The test is whether or not a party had "ample opportunity" to investigate the truth of the representations, regardless of whether or not the party actually investigated. *Smith*, 144 Ill.App.3d at 174, 494 N.E.2d at 866; *Thrall*, 145 Ill.App. 3d at 117, 495 N.E.2d at 1135; *Luciani*, 106 Ill.App.3d at 884, 436 N.E.2d at 256.

In this case, the Seventh Circuit ignored the foregoing law on justifiable reliance instead choosing to analyze it as part of the comparative negligence defense.[4] Under its

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[4] The Seventh Circuit states that petitioner conceded at oral argument that he intended to induce the respondent's reliance

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4 *(Continued)*

as shown by his addressing the letter to the respondent (see p. 6a, *infra*). No such concession was made, and the dialogue at oral argument on this subject was as follows:

> JUDGE POSNER: . . . He wrote the letter to Greycas, and he makes these representations, and does he not intend that those representations will influence Greycas to make the loan? That's implicit when you say he was trying to help his client to get a loan. Making representations to Greycas in hopes of influencing Greycas to make the loan.
>
> COUNSEL: It is true that that letter was addressed to Greycas and he *knew* that Greycas would rely on it, and I believe that he testified to that.
>
> JUDGE POSNER: And he intended to induce reliance? Otherwise, there would be no purpose in writing the letter.
>
> COUNSEL: He *knew* that Greycas would rely and that testimony stands in the record. However, your honor, the question is: who's relying on the borrower? Everybody is in this situation. Does the lender, as a matter of law, have a right for three weeks, when it is represented by its own attorneys, to do nothing. And at the end of the day, on the day the monies are going to be dispersed. . .
>
> JUDGE POSNER: Well, what's the purpose of getting the letter from Proud if you're not going to rely on it?
>
> COUNSEL: Because. . . .
>
> JUDGE POSNER: There are [unintelligible]. . .
>
> COUNSEL: No, your honor, because there are two purposes for that letter. One is that Mr. Proud said "I am the attorney for the borrower. I have read this loan agreement and its provisions are binding and enforceable." The lender in this case wanted to have it both ways. . .

(emphasis added). The only "concession" made by the petitioner was that he knew respondent would rely. Mere knowledge that a non-client may rely is insufficient to give rise to a duty. *York v. Stiefel*, 99 Ill.2d 312, 320, 458 N.E.2d 488, 494 (1983) (no duty owed, despite attorney's knowledge that his clients' wives would rely on his advice in signing away rights to marital homes); *cf.*,

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analysis, the respondent was not obligated to inquire as to the truth of the representations, calling such requirement a duplicative effort (see, p.11a, *infra*). The Seventh Circuit made an analogy to an automobile accident, stating that superior method of accident avoidance is not driving recklessly, and that a pedestrian has no obligation to wear armor in anticipation of reckless driving (see, p. 10a-11a, *infra*). This analogy is inapposite under the legal theories and facts presented in this case. The respondent's attorneys were obligated to "wear armor" as it were, to protect their own client's interest as the client itself recognized by ordering its own attorneys to conduct the title search. A person cannot enter into a transaction with his eyes closed to available information and then claim that he has been deceived by another. *Central States*, 117 Ill.App.3d at 607, 453 N.E.2d at 937.

Since all U.C.C. statements are public records (Ill.Rev.Stat. (1985) ch. 26, ¶ 9-401) and a person is presumed to know that which is a public record (*Chas. Hester Enterprises, Inc. v. Illinois Founders Ins. Co.*, 114 Ill.2d 278, 292, 499 N.E.2d 1319, 1325 (1986)), respondent cannot show that its reliance on petitioner was justified. These public documents were equally accessible to both attorneys in this loan transaction. The respondent's attorney only had to telephone the recorder's office in order to protect his own client's interest and fulfill the directive to conduct the title search. To file their client's lien, the respondent's attorney simply had to mail the filing statement, which he had prepared, to the recorder's office. Instead, the respondent's attorney prepared all documents and mailed them not

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4 *(Continued)*

Popp v. Dyslin, 149 Ill.App.3d 956, 964, 500 N.E.2d 1039, 1044 (1986) (court found no duty against a bank under a third party beneficiary theory, holding, "it is not enough that the parties to the contract know, expect or even intend that others will benefit. The contract must be undertaken for plaintiff's direct benefit.")

to the recorder's office and not even to the borrower's attorney, on whom respondent later claimed to rely, but to the borrower himself, who then substituted the list of collateral equipment before filing the financing statement.[5]

It is clear that the foregoing Illinois principles were not applied as to the essential element of justifiable reliance, in disregard of this Court's holding in *Erie R.R. Co. v. Thompkins*.

C. A Plaintiff Cannot Recover Until Actual Damages Have Been Sustained.

The final element to which the Seventh Circuit did not apply Illinois law relates to damages. In this case, the respondent had pending actions against the estate and against the borrower's wife, who was a cosigner on all the loan documents.

In Illinois, an action may not be maintained until actual damages have been sustained. A legal malpractice action is premature if the plaintiff has a pending or viable cause of action in which he may still recover damages. *Schulte v. Burch*, 151 Ill.App.3d 332, 336, 502 N.E.2d 856, 862 (1986); *Austin's Rack, Inc. v. Gordon & Glickson, P.C.*, 145 Ill.App.3d 500, 503, 495 N.E.2d 1137, 1139 (1986); *Bartholomew v. Crockett*, 131 Ill.App.3d 456, 465-66, 475 N.E.2d 1035, 1041-42 (1985).

Although the Seventh Circuit recognized this rule of law when it noted that if the respondent had hopes of recovering from its other pending claims, "there would be a serious question of whether it actually sustained the full damages that it is seeking in this action," it then finds that there is no clear error in the district court's finding for the

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[5] The Seventh Circuit's opinion make a misstatement of fact as to how the letter signed by the petitioner was delivered to respondent. It was not mailed, as the Seventh Circuit stated (see p. 2a, *infra*), but was hand-delivered by the borrower himself.

respondent (see p. 15a, *infra*). However, the district court made no findings as to the other pending claims that the respondent has against the co-borrower and the estate.

The evidence established that the respondent could not show that it had yet to incur actual damages at trial and, because damages are a necessary element of any cause of action, the respondent could not recover from the petitioner. Illinois law as to this essential element also was not followed.

III.

A PRIOR STATE COURT JUDGMENT WAS GIVEN PRECLUSIVE EFFECT IN VIOLATION OF 28 U.S.C. § 1728 AND THE DOCTRINE OF COLLATERAL ESTOPPEL

The respondent in this action sought to prove the essential element of damages by offering into evidence a prior state court judgment in which certain creditors' priority positions as to the collateral equipment had been adjudicated. Under Illinois law, because the petitioner was not party, nor a privity, to the prior state court action, offensive use of collateral estoppel was erroneous, and the judgment was not admissible as evidence of the respondent's damages, the claimed loss of the collateral equipment. In accepting this judgment into evidence, the court violated 28 U.S.C. § 1738, since it gave the judgment more than "full faith and credit," according it greater effect than the state court would have.

The doctrine of collateral estoppel precludes relitigation of issues actually litigated in a prior action. *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326, n. 5 (1979). Offensive use of this doctrine occurs when the plaintiff seeks to prevent the defendant from relitigating an issue already lost in a prior action. *Parklane*, 439 U.S. at 329. The requirements which must be met before this doctrine may be applied are: 1) the party, or his privity, against whom estoppel is asserted, was a party to that prior suit; 2) the

same factual issue must be presented in both suits and must have been specifically decided, although the legal theories may differ; and 3) the defendant had a full and fair opportunity to litigate. *Allen v. McCurry*, 449 U.S. 90, 94-95 (1980); *Housing Authority v. Y.M.C.A.*, 101 Ill.2d 246, 255, 461 N.E.2d 959 (1984); *Raper v. Hazelett & Erdal* 114 Ill.App.3d 649, 652, 449 N.E. 2d 268, 270 (1983). When these factors are applied to this case, it is clear that the state court judgment was erroneously admitted into evidence and given preclusive effect against the petitioner in violation of Illinois law and his due process rights.

First, the petitioner was not a party to the prior action nor was he in privity with the borrower, because the petitioner did not have any rights to the subject property. *Oak Brook Bank v. Hawthorne Bank*, 90 Ill.App.3d 642, 645, 413 N.E.2d 491, 494 (1980). "Privity contemplates a mutual or successive relationship to the same property rights which were the subject matter of prior litigation." *Sweeting v. Campbell*, 2 Ill.2d 491, 496, 119 N.E.2d 237, 240 (1954).

This first element could not be met under Illinois law. In *Oak Brook Bank*, the plaintiff-lender had made a loan to borrowers, not parties to the first suit, secured by certain real estate. The defendant was the land trustee of the property. After the loan, the plaintiff gave defendant notice of the transaction and gave instructions not to convey property without the plaintiff-lender's consent. The plantiff sued the borrower in the first suit and obtained judgment. The defendant in the second suit conveyed the property after the entry of judgment on the borrower's directions, without notice to the plaintiff. Thereafter, the lender settled the other suit with the plaintiff and filed a "satisfaction release of judgment." The plaintiff-lender then sued the defendant for the difference of the amount owed and the amount recovered from the borrowers. 90 Ill.App.3d at 644-45, 413 N.E.2d at 493-94. The court refused to hold the plaintiff bound by the prior judgment because the defend-

ant was not a party, nor in privity with a party in the first lawsuit. Likewise, in this case, there was no privity because petitioner had no relationship nor rights to the subject property.

Nor was the third factor, a full and fair opportunity to litigate, afforded to petitioner in this suit. The failure to meet this element is sufficient to bar application of the doctrine. *Allen*, 449 U.S. at 95; *Fred Olson Motors Serv. v. Container Corp.*, 81 Ill.App.3d 825, 829-30, 401 N.E.2d 1098, 1101 (1980). A full and fair opportunity to litigate is defined by due process standards and includes the right to present evidence, cross examine and rebut the evidence. *Kremer v. Chem. Const. Co.*, 456 U.S. 461, 481-83, *reh. denied*, 458 U.S. 1133 (1982); *see also*, *Fred Olson Motor Serv.*, 81 Ill.App.3d at 830, 401 N.E.2d at 1101-02.

The Seventh Circuit attempted to avoid the foregoing law on this issue. It first noted "it is a little hard to understand why [judgments] should not be allowed to have merely evidentiary effect, if for some reason not all of the requirements of res judicata or collateral estoppel are fulfilled" (see, p. 12a, *infra).* It was then unsure whether the rule that judgments are inadmissible should apply where there is a bench trial (see, pp. 12a-13a, *infra*). It then held that the state court judgment was evidence of the status of the respondent's lien and was admissible (see, p. 13a, *infra*).

This analysis is simply wrong under Illinois law. The case relied upon by the Seventh Circuit, *Sanitary Dist. v. U.S.F. & G. Co.*, 392 Ill. 602, 611-12, 65 N.E.2d 364, 368 (1946) does not stand for the proposition that prior state court judgments are admissible. Rather, this case involved a suit against a surety seeking payment of a judgment entered against the plaintiff on a performance bond. The issue was whether the bond covered the type of activities which were the subject of the prior litigation, i.e. the use of explosives. 392 Ill. at 611-13, 65 N.E.2d at 368.

The Illinois Supreme Court held that the judgment was admissible for the limited purpose of showing the liability on which the claims of the plaintiff's in the prior suit were based and upon which judgment was entered. 392 Ill. at 611, 65 N.E.2d at 368-69. The court came to this conclusion noting that defendant was in privity, had proper notice of the pendency of the prior action, and demand was made to defend the plaintiff which defendant had declined. 392 Ill. at 612, 65 N.E.2d at 369. The court further found that under the terms of the bond, any judgment would be conclusive against the surety as to the amount, liability and all other issues pertaining to the judgment. 392 Ill. at 614, 65 N.E.2d at 369.

The decision in *Sanitary District* only stands for the proposition that if liability rests on derivative responsibility, such as with sureties, indemnitors, or insurers, then collateral estoppel may apply. *Cowen v. Ins. Co. of North America*, 22 Ill.App.3d 883, 890, 318 N.E.2d 315, 321 (1974). No Illinois case has ever taken this holding outside of this proposition, and none have ever cited to *Sanitary District* for the proposition that judgments are binding on a non-party or that they are admissible. *See, Karas v. Snell*, 11 Ill.2d 233, 246, 142 N.E.2d 46, 54 (1957); *Bassick Co. v. Mississippi Valley Erection Co.*, 104 Ill.App.3d 517, 521, 432 N.E.2d 1146, 1149 (1982); *Tenenbaum v. Chicago*, 11 Ill.App.3d 987, 1010, 297 N.E.2d 716, 730 (1973), *rev'd in part and aff'd in part on other grounds*, 60 Ill.2d 363, 325 N.E.2d 607 (1975); *Apex Mut. Ins. Co. v. Christner*, 99 Ill.App.2d 153, 161, 240 N.E.2d 742, 747 (1968); *True v. Civil Serv. Com'n.*, 350 Ill.App. 248, 250, 112 N.E.2d 519, 519 (1953). Two cases cite to *Sanitary District* for the proposition that the defendants were not bound by the prior judgment because they were denied the opportunity to litigate the issue. *See, Sec. Ins. Co. v. Mato*, 13 Ill.App.3d 11, 17, 298 N.E.2d 725, 730 (1973); *Palmer v. Mitchell*, 57 Ill.App.2d 160, 168, 206 N.E.2d 776, 779 (1965).

When the issues concern title and ownership, as in this case, state court judgments are not admissible in Illinois to show who has title unless one was party to the prior action. *Sweeting v. Campbell*, 2 Ill.2d 491, 498, 119 N.E.2d 237, 240-41 (1954). In *Sweeting*, a defendant who was not party to the prior suit was not bound by the prior adjudication and the judgment was only admissible against those persons who were parties to the prior suit. 2 Ill.2d at 498, 119 N.E.2d at 240-41. The court rejected the argument that the second adjudication may reach an inconsistent result noting that the overriding principle was "that every litigant shall have his day in court." 2 Ill.2d at 491, 119 N.E.2d at 241.

The Seventh Circuit also relied on Fed.R.Evid. 803(24), the catch-all exception to the hearsay rule, and Fed.R.Evid. 803(14) which provides that records purporting to establish interest in property is an exception to the hearsay rule and is "proof of the content of the original recorded document and its execution and delivery" (see, pp. 12a-13a, *infra*). On its face, Rule 803(14) applies to documents which would be filed in a recorder's office, such as documents showing conveyance of property. The respondent never submitted proof of the other creditor's filed financing statements, which would have been not only admissible under this rule, but also probative of the question of who had first priority.

The Seventh Circuit's reliance on these rules does not cure the major problem presented in this case: that the petitioner had no opportunity to litigate the issue. Further, the Seventh Circuit misconstrues the district court's finding on this issue in stating the judgment was merely evidence which could be rebutted. The district court found:

> The equipment in question and the rights of parties having a claim thereto, including plaintiff, were the subject matter of a cause of action in the Circuit Court of Fayette County, docketed in said court as Cause No. 82-Ch-11. As a result of

> the judgment entered in said cause, plaintiff lost the value of the collateral upon which it relied in making its loan, to the extent found herein.

(see, p.20a, *infra*). It is clear by this finding that the district court gave preclusive effect to the judgment as to the respondent's claimed damages. The preclusive effect is also evidenced by comparing the findings in the judgment with the index book of the Recorder of Deeds, also admitted into evidence. The judgment found that two creditors, Equico and John Deere, had a higher priority than the respondent's as to most of the equipment. However, the Recorder's index book does not show the name Equico at all and John Deere's sole interest was on unidentified equipment.

This court should exercise its supervisory authority and accept this petition to determine the important questions presented as to this issue, including whether prior adjudications are admissible as evidence and whether offensive use of the doctrine of collateral estoppel was proper where the petitioner was not in privity, and was deprived of his basic due process right to litigate the issue of damages.

CONCLUSION

For the foregoing reasons, this petition for writ of certiorari should be granted, and this Court should give this matter its plenary consideration.

Respectfully submitted,

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November 30, 1987

APPENDIX

In the
United States Court of Appeals
For the Seventh Circuit

No. 86-2340

GREYCAS, INC.,

Plaintiff-Appellee,

v.

THEODORE S. PROUD,

Defendant-Appellant.

Appeal from the United States District Court
for the Southern District of Illinois, Alton Division.
No. 82 C 5138—**William L. Beatty**, *Judge.*

ARGUED FEBRUARY 17, 1987—DECIDED AUGUST 3, 1987

Before BAUER, *Chief Judge*, and CUMMINGS and POSNER, *Circuit Judges.*

POSNER, *Circuit Judge.* Theodore S. Proud, Jr., a member of the Illinois bar who practices law in a suburb of Chicago, appeals from a judgment against him for $833,760, entered after a bench trial. The tale of malpractice and misrepresentation that led to the judgment begins with Proud's brother-in-law, Wayne Crawford, like Proud a lawyer but one who devoted most of his attention to a large farm that he owned in downstate Illinois. The farm fell on hard times and by 1981 Crawford was in dire financial straits. He had pledged most of his farm machinery to lenders, yet now desperately needed more money. He approached Greycas, Inc., the plaintiff in this case, a large

financial company headquartered in Arizona, seeking a large loan that he offered to secure with the farm machinery. He did not tell Greycas his financial difficulties or that he had pledged the machinery to other lenders, but he did make clear that he needed the loan in a hurry. Greycas obtained several appraisals of Crawford's farm machinery but did not investigate Crawford's financial position or discover that he had pledged the collateral to other lenders, who had perfected their liens in the collateral. Greycas agreed to lend Crawford $1,367,966.50, which was less than the appraised value of the machinery.

The loan was subject, however, to an important condition, which is at the heart of this case: Crawford was required to submit a letter to Greycas, from counsel whom he would retain, assuring Greycas that there were no prior liens on the machinery that was to secure the loan. Crawford asked Proud to prepare the letter, and he did so, and mailed it to Greycas, and within 20 days of the first contact between Crawford and Greycas the loan closed and the money was disbursed. A year later Crawford defaulted on the loan; shortly afterward he committed suicide. Greycas then learned that most of the farm machinery that Crawford had pledged to it had previously been pledged to other lenders.

The machinery was sold at auction. The Illinois state court that determined the creditors' priorities in the proceeds of the sale held that Greycas did not have a first priority on most of the machinery that secured its loan; as a result Greycas has been able to recover only a small part of the loan. The judgment it obtained in the present suit is the district judge's estimate of the value that it would have realized on its collateral had there been no prior liens, as Proud represented in his letter.

That letter is the centerpiece of the litigation. Typed on the stationery of Proud's firm and addressed to Greycas, it identifies Proud as Crawford's lawyer and states that, "in such capacity, I have been asked to render my opinion in connection with" the proposed loan to Craw-

ford. It also states that "this opinion is being delivered in accordance with the requirements of the Loan Agreement" and that

> I have conducted a U.C.C., tax, and judgment search with respect to the Company [i.e., Crawford's farm] as of March 19, 1981, and except as hereinafter noted all units listed on the attached Exhibit A ("Equipment") are free and clear of all liens or encumbrances other than Lender's perfected security interest therein which was recorded March 19, 1981 at the Office of the Recorder of Deeds of Fayette County, Illinois.

The reference to the lender's security interest is to Greycas's interest; Crawford, pursuant to the loan agreement, had filed a notice of that interest with the recorder. The excepted units to which the letter refers are four vehicles. Exhibit A is a long list of farm machinery—the collateral that Greycas thought it was getting to secure the loan, free of any other liens. Attached to the loan agreement itself, however, as Exhibit B, is another list of farm machinery constituting the collateral for the loan, and there are discrepancies between the two lists; more on this later.

Proud never conducted a search for prior liens on the machinery listed in Exhibit A. His brother-in-law gave him the list and told him there were no liens other than the one that Crawford had just filed for Greycas. Proud made no effort to verify Crawford's statement. The theory of the complaint is that Proud was negligent in representing that there were no prior liens, merely on his brother-in-law's say-so. No doubt Proud *was* negligent in failing to conduct a search, but we are not clear why the *misrepresentation* is alleged to be negligent rather than deliberate and hence fraudulent, in which event Greycas's alleged contributory negligence would not be an issue (as it is, we shall see), since there is no defense of contributory or comparative negligence to a deliberate tort, such as fraud. See, e.g., *Cenco Inc. v. Seidman & Seidman*, 686 F.2d 449, 454 (7th Cir. 1982) (Illinois law); cf. *Team-*

sters Local 282 Pension Trust Fund v. Angelos, 762 F.2d 522, 528-29 (7th Cir. 1985). Proud did not merely say, "There are no liens"; he said, "I have conducted a U.C.C., tax, and judgment search"; and not only is this statement, too, a false one, but its falsehood cannot have been inadvertent, for Proud knew he had not conducted such a search. The concealment of his relationship with Crawford might also support a charge of fraud. But Greycas decided, for whatever reason, to argue negligent misrepresentation rather than fraud. It may have feared that Proud's insurance policy for professional malpractice excluded deliberate wrongdoing from its coverage, or may not have wanted to bear the higher burden of proving fraud, or may have feared that an accusation of fraud would make it harder to settle the case—for most cases, of course, are settled, though this one has not been. In any event, Proud does not argue that either he is liable for fraud or he is liable for nothing.

He also does not, and could not, deny or justify the misrepresentation; but he argues that it is not actionable under the tort law of Illinois, because he had no duty of care to Greycas. (This is a diversity case and the parties agree that Illinois tort law governs the substantive issues.) He argues that Greycas had an adversarial relationship with Proud's client, Crawford, and that a lawyer has no duty of straight dealing to an adversary, at least none enforceable by a tort suit. In so arguing, Proud is characterizing Greycas's suit as one for professional malpractice rather than negligent misrepresentation, yet elsewhere in his briefs he insists that the suit was solely for negligent misrepresentation—while Greycas insists that its suit charges both torts. Legal malpractice based on a false representation, and negligent misrepresentation by a lawyer, are such similar legal concepts, however, that we have great difficulty both in holding them apart in our minds and in understanding why the parties are quarreling over the exact characterization; no one suggests, for example, that the statute of limitations might have run on one but not the other tort. So we shall discuss both.

Proud is undoubtedly correct in arguing that a lawyer has no general duty of care toward his adversary's client; it would be a considerable and, as it seems to us, an undesirable novelty to hold that every bit of sharp dealing by a lawyer gives rise to prima facie tort liability to the opposing party in the lawsuit or negotiation. The tort of malpractice normally refers to a lawyer's careless or otherwise wrongful conduct toward his own client. Proud argues that Crawford rather than Greycas was his client, and although this is not so clear as Proud supposes—another characterization of the transaction is that Crawford undertook to obtain a lawyer for Greycas in the loan transaction—we shall assume for purposes of discussion that Greycas was not Proud's client.

Therefore if malpractice just meant carelessness or other misconduct toward one's own client, Proud would not be liable for malpractice to Greycas. But in *Pelham v. Griesheimer*, 92 Ill. 2d 13, 440 N.E.2d 96 (1982), the Supreme Court of Illinois discarded the old common law requirement of privity of contract for professional malpractice; so now it is possible for someone who is not the lawyer's (or other professional's) client to sue him for malpractice. The court in *Pelham* was worried, though, about the possibility of a lawyer's being held liable "to an unlimited and unknown number of potential plaintiffs," *id.* at 20, 440 N.E.2d at 99, so it added that "for a nonclient to succeed in a negligence action against an attorney, he must prove that the primary purpose and intent of the attorney-client relationship itself was to benefit or influence the third party," *id.* at 21, 440 N.E.2d at 100. That, however, describes this case exactly. Crawford hired Proud not only for the primary purpose, but for the sole purpose, of influencing Greycas to make Crawford a loan. The case is much like *Brumley v. Touche, Ross & Co.*, 139 Ill. App. 3d 831, 836, 487 N.E.2d 641, 644-45 (1985), where a complaint that an accounting firm had negligently prepared an audit report that the firm knew would be shown to an investor in the audited corporation and relied on by that investor was held to state a claim for professional

malpractice. In *Conroy v. Andeck Resources '81 Year-End Ltd.*, 137 Ill. App. 3d 375, 389-91, 484 N.E.2d 525, 536-37 (1985), in contrast, a law firm that represented an offeror of securities was held not to have any duty of care to investors. The representation was not intended for the benefit of investors. Their reliance on the law firm's using due care in the services it provided in connection with the offer was not invited. Cf. *Barker v. Henderson, Franklin, Starnes & Holt*, 797 F.2d 490, 497 (7th Cir. 1986).

All this assumes that *Pelham* governs this case, but arguably it does not, for Greycas, as we noted, may have decided to bring this as a suit for negligent misrepresentation rather than professional malpractice. We know of no obstacle to such an election; nothing is more common in American jurisprudence than overlapping torts.

The claim of negligent misrepresentation might seem utterly straightforward. It might seem that by addressing a letter to Greycas intended (as Proud's counsel admitted at argument) to induce reliance on the statements in it, Proud made himself prima facie liable for any material misrepresentations, careless or deliberate, in the letter, whether or not Proud was Crawford's lawyer or for that matter anyone's lawyer. Knowing that Greycas was relying on him to determine whether the collateral for the loan was encumbered and to advise Greycas of the results of his determination, Proud negligently misrepresented the situation, to Greycas's detriment. But merely labeling a suit as one for negligent misrepresentation rather than professional malpractice will not make the problem of indefinite and perhaps excessive liability, which induced the court in *Pelham* to place limitations on the duty of care, go away. So one is not surprised to find that courts have placed similar limitations on suits for negligent misrepresentation—so similar that we are led to question whether, as suggested in *HGN Corp. v. Chamberlain, Hrdlicka, White, Johnson & Williams*, 642 F. Supp. 1443, 1452-53 (N.D. Ill. 1986), these really are different torts, at least when both grow out of negligent misrepresentations by

lawyers. For example, the *Brumley* case, which we cited earlier, is a professional-malpractice case, yet it has essentially the same facts as *Ultramares Corp. v. Touche, Niven & Co.*, 255 N.Y. 170, 174 N.E. 441 (1931), where the New York Court of Appeals, in a famous opinion by Judge Cardozo, held that an accountant's negligent misrepresentation was not actionable at the suit of a lender who had relied on the accountant's certified audit of the borrower.

The absence of a contract between the lender and the accountant defeated the suit in *Ultramares*—yet why should privity of contract have been required for liability just because the negligence lay in disseminating information rather than in designing or manufacturing a product? The privity limitation in products cases had been rejected, in another famous Cardozo opinion, years earlier. See *MacPherson v. Buick Motor Co.*, 217 N.Y. 382, 111 N.E. 1050 (1916). Professor Bishop suggests that courts were worried that imposing heavy liabilities on producers of information might cause socially valuable information to be underproduced. See *Negligent Misrepresentation Through Economists' Eyes*, 96 L.Q. Rev. 360 (1980). Many producers of information have difficulty appropriating its benefits to society. The property-rights system in information is incomplete; someone who comes up with a new idea that the law of intellectual property does not protect cannot prevent others from using the idea without reimbursing his costs of invention or discovery. So the law must be careful not to weigh these producers down too heavily with tort liabilities. For example, information produced by securities analysts, the news media, academicians, and so forth is socially valuable, but as its producers can't capture the full value of the information in their fees and other remuneration, the information may be underproduced. Maybe it is right, therefore—or at least efficient—that none of these producers should have to bear the full costs. (Similar reasoning may explain the tort immunity, now largely abrogated, of charitable enterprises, and the tort immunities of public officers. See *Colaizzi v. Walker*, 812

F.2d 304, 308 (7th Cir. 1987); *Carson v. Block*, 790 F.2d 562, 564 (7th Cir. 1986).) At least that was once the view; and while *Ultramares* has now been rejected, in Illinois as elsewhere—maybe because providers of information are deemed more robust today than they once were or maybe because it is now believed that auditors, surveyors, and other providers of professional services were always able to capture the social value of even the information component of those services in the fees they charged their clients—a residuum of concern remains. So when in *Rozny v. Marnul*, 43 Ill. 2d 54, 250 N.E.2d 656 (1969), the Supreme Court of Illinois, joining the march away from *Ultramares*, held for the first time that negligent misrepresentation was actionable despite the absence of a contract, and thus cast aside the same "privity of contract" limitation later overruled with regard to professional malpractice in *Pelham*, the court was careful to emphasize facts in the particular case before it that limited the scope of its holding—facts such as that the defendant, a surveyor, had placed his "absolute guarantee for accuracy" on the plat and that only a few persons would receive and rely on it, thus limiting the potential scope of liability. See *id.* at 67-68, 250 N.E.2d at 663.

Later Illinois cases, however, influenced by section 552 of the Second Restatement of Torts (1977), state the limitation on liability for negligent misrepresentation in more compact terms—as well as in narrower scope—than *Rozny*. These are cases in the intermediate appellate court, but, as we have no reason to think the Supreme Court of Illinois would reject them, we are bound to follow them. See *Williams, McCarthy, Kinley, Rudy & Picha v. Northwestern National Ins. Group*, 750 F.2d 619, 624 (7th Cir. 1984). They hold that "one who in the course of his business or profession supplies information for the guidance of others in their business transactions" is liable for negligent misrepresentations that induce detrimental reliance. *Penrod v. Merrill Lynch, Pierce, Fenner & Smith*, 68 Ill. App. 3d 75, 81-82, 385 N.E.2d 376, 381 (1979); see also *Perschall v. Raney*, 137 Ill. App. 3d 978, 983, 484 N.E.2d

1286, 1289 (1985); Prosser and Keeton on the Law of Torts § 107, at p. 747 (5th ed. 1984). Whether there is a practical as distinct from a merely semantic difference between this formulation of the duty limitation and that of *Pelham* may be doubted but cannot change the outcome of this case. Proud, in the practice of his profession, supplied information (or rather misinformation) to Greycas that was intended to guide Greycas in commercial dealings with Crawford. Proud therefore had a duty to use due care to see that the information was correct. He used no care.

Proud must lose on the issue of liability even if the narrower, *ad hoc* approach of *Rozny* is used instead of the approach of section 552 of the Restatement. Information about the existence of previous liens on particular items of property is of limited social as distinct from private value, by which we mean simply that the information is not likely to be disseminated widely. There is consequently no reason to give it special encouragement by overlooking carelessness in its collection and expression. Where as in this case the defendant makes the negligent misrepresentation directly to the plaintiff in the course of the defendant's business or profession, the courts have little difficulty in finding a duty of care. Prosser and Keeton on the Law of Torts, *supra*, § 107, at p. 747.

There is no serious doubt about the existence of a causal relationship between the misrepresentation and the loan. Greycas would not have made the loan without Proud's letter. Nor would it have made the loan had Proud advised it that the collateral was so heavily encumbered that the loan was as if unsecured, for then Greycas would have known that the probability of repayment was slight. Merely to charge a higher interest rate would not have been an attractive alternative to security; it would have made default virtually inevitable by saddling Crawford with a huge fixed debt. To understand the astronomical interest rate that is required to make an unsecured loan a paying proposition to the lender when the risk of default is high, notice that even if the riskless interest rate is only

3 percent, the rate of inflation zero, the cost of administering the loan zero, and the lender risk-neutral, he still must charge an annual interest rate of 106 percent if he thinks there is only a 50 percent chance that he will get his principal back.

Proud argues, however, that his damages should be reduced in recognition of Greycas's own contributory negligence, which, though no longer a complete defense in Illinois, is a partial defense, renamed "comparative negligence." *Alvis v. Ribar*, 85 Ill. 2d 1, 421 N.E.2d 886 (1981); see *Wolkenhauer v. Smith*, No. 86-2859, slip op. at 11 (7th Cir. June 24, 1987). It is as much a defense to negligent misrepresentation as to any other tort of negligence. *Luciani v. Bestor*, 106 Ill. App. 3d 878, 889, 436 N.E.2d 251, 260 (1982); *McAfee v. Rockford Coca-Cola Bottling Co.*, 40 Ill. App. 3d 521, 526, 352 N.E.2d 50, 55 (1976); Prosser and Keeton on the Law of Torts, *supra*, § 108, at p. 750. On the issue of comparative negligence the district court said only that "defendant may have proved negligence upon the part of plaintiff but that negligence, if any, had no causal relationship to the malpractice of the defendant or the damages to the plaintiff." This comment is not easy to fathom. If Greycas was careless in deciding whether to make the loan, this implies that a reasonable investigation by Greycas would have shown that the collateral for the loan was already heavily encumbered; knowing this, Greycas would not have made the loan and therefore would not have suffered any damages.

But we think it too clear to require a remand for further proceedings that Proud failed to prove a want of due care by Greycas. Due care is the care that is optimal given that the other party is exercising due care. See *McCarty v. Pheasant Run, Inc.*, No. 86-2135, slip op. at 6 (7th Cir. July 22, 1987); *Davis v. Consolidated Rail Corp.*, 788 F.2d 1260, 1265 (7th Cir. 1986) (both cases applying Illinois law). It is not the higher level of care that would be optimal if potential tort victims were required to assume that the rest of the world was negligent. A

pedestrian is not required to exercise a level of care (e.g., wearing a helmet or a shin guard) that would be optimal if there were no sanctions against reckless driving. Otherwise drivers would be encouraged to drive recklessly, and knowing this pedestrians would be encouraged to wear helmets and shin guards. The result would be a shift from a superior method of accident avoidance (not driving recklessly) to an inferior one (pedestrian armor).

So we must ask whether Greycas would have been careless not to conduct its own UCC search had Proud done what he had said he did—conduct his own UCC search. The answer is no. The law normally does not require duplicative precautions unless one is likely to fail or the consequences of failure (slight though the likelihood may be) would be catastrophic. One UCC search is enough to disclose prior liens, and Greycas acted reasonably in relying on Proud to conduct it. Although Greycas had much warning that Crawford was in financial trouble and that the loan might not be repaid, that was a reason for charging a hefty interest rate and insisting that the loan be secured; it was not a reason for duplicating Proud's work. It is not hard to conduct a UCC lien search; it just requires checking the records in the recorder's office for the county where the debtor lives. See Ill. Rev. Stat. ch. 26, ¶ 9-401. So the only reason to backstop Proud was if Greycas should have assumed he was careless or dishonest; and we have just said that the duty of care does not require such an assumption. Had Proud disclosed that he was Crawford's brother-in-law this might have been a warning signal that Greycas could ignore only at its peril. To go forward in the face of a known danger is to assume the risk. See, e.g., *Davis v. Consolidated Rail Corp.*, *supra*, 788 F.2d at 1266-67 (Illinois law); *Phillips v. Croy*, 173 Ind. App. 401, 405, 363 N.E.2d 1283, 1285 (1977). But Proud did not disclose his relationship to Crawford.

The last issue concerns the amount of damages awarded Greycas. In estimating what Proud's negligence had cost Greycas, the judge relied heavily on the state court's find-

ing that Greycas's lien was subordinate to other liens. Proud complains that it was wrong to give collateral estoppel effect to a finding in a case to which he was not a party. But we do not understand the district judge to have been using the judgment to prevent further inquiry into the question of Greycas's damages. The state court's judgment determining the priority of the liens was merely some evidence of the degree to which Proud's misconduct had injured Greycas; for the injury depended on the size of the perfected liens that were prior to its lien. No one tried to prevent Proud from proving, if he could, that the judgment in the state court was erroneous and that Greycas's lien had actually enjoyed the priority that Proud had represented it to have. Proud offered no such evidence. His attack on the state court judgment must fail.

We are aware that, with immaterial exceptions, see Fed. R. Evid. 803(23); Clayton Act § 5(a), 15 U.S.C. § 16(a), civil judgments are said not to be usable in subsequent proceedings as evidence of the facts underlying the judgment; for as to those facts, the judgment is hearsay. See 4 Weinstein's Evidence ¶ 803(22)[01], at 803-353 (1985); McCormick on Evidence § 318, at p. 894 (3d ed. 1984). Since judgments are often given conclusive effect in subsequent litigation, through the doctrines of res judicata and collateral estoppel, it is a little hard to understand why they should not be allowed to have merely evidentiary effect, if for some reason not all the requirements of res judicata or collateral estoppel are fulfilled. A practical reason for denying them evidentiary effect is, however, the difficulty of weighing a judgment, considered as evidence, against whatever contrary evidence a party to the current suit might want to present. The difficulty must be especially great for a jury, which is apt to give exaggerated weight to a judgment. The analytical difficulties posed by efforts to use a judgment as evidence are, however, the only good reasons offered for the rule (others are canvassed in McCormick on Evidence, *supra*, § 318, at p. 894), and as they are of less or no force where, as in this case, the trial is not to a jury, we are not sure

the rule should apply in such cases. A further point is that a judgment, insofar as it fixes property rights, should be admissible as the official record of such rights, just like other documents of title, on which see Fed. R. Evid. 803(14); *Sanitary District v. U.S. Fidelity & Guaranty Co.*, 392 Ill. 602, 611-12, 65 N.E.2d 364, 368 (1946). That was the use made of it by Greycas and the district judge: the state court judgment fixed Greycas's rights, equivalent to title, in Crawford's farm machinery. In addition, there is always the catch-all exception to the hearsay rule to fall back on. See Fed. R. Evid. 803(24). "A [hearsay] statement not specifically covered by any of the foregoing exceptions but having equivalent circumstantial guarantees of trustworthiness" is admissible, subject to conditions that in fact are satisfied here.

There is still another path to the same conclusion: it should make no difference to Greycas's rights against Proud whether the state court judgment is erroneous. And if that is irrelevant, then the judgment is not being offered as hearsay at all. Greycas should not be penalized because a state court may have found the previous liens to be even more extensive than Proud's search, if he had conducted a search, would have revealed. If the injury to Greycas was a joint act of Proud and the state court, Proud is fully liable under conventional principles. If the state court judgment had been made up out of whole cloth—if there had been no prior liens when Greycas's lien was filed—then the search would have turned up nothing, and it could be argued therefore that Greycas would have gone ahead and have made the loan and have been burned just as badly as it was, but through no fault of Proud. But Proud was free to show this, since the state court judgment was put in merely as evidence of the status of Greycas's liens; and it was admissible for that purpose.

There are, finally, the discrepancies not only between Exhibit A and Exhibit B, but between those two exhibits on the one hand and the list of machinery attached to the state court's judgment fixing the priority of liens on the other. The judge resolved the first set of discrepan-

cies by refusing to allow Greycas to claim damages with respect to any piece of machinery not on both lists. He resolved the second—and this is the focus of Proud's protest—on the basis of summaries prepared by Greycas's lawyers which purport to identify the same items on both lists, even though the items are sometimes called by different names (e.g., "sprayer" and "spreader"). Proud complains that the summaries did not meet the test for admissibility of summaries in the Federal Rules of Evidence. See Rule 1006. Such a complaint has a hollow ring in a bench trial. A district judge can be trusted in general, and in this particular instance, to give evidence its proper weight without regard to the technical rules of evidence, see McCormick on Evidence, *supra*, § 60, at pp. 153-54, which insofar as they relate to matters of probative force rather than to privilege are designed primarily for the control of juries. The summaries are basically just a matching of the descriptions in the two lists. They made it easier for the judge to compare the descriptions of each pair of items and decide whether they were probably referring to the same piece of machinery, only differently described. We can find no clear error in his comparisons.

Proud complains because the judge, in valuing the items, used the highest of three appraisals that Greycas had obtained before making the loan. The judge then subtracted 20 percent of that value, on the theory that that was the best estimate of the depreciation of the machinery between the date of the appraisal and the date of Crawford's default. He refused to use the price obtained at the auction, conducted six months after the default; that price was much lower. It is possible to argue that the appraisal the judge used was too high, or the 20 percent depreciation figure too low, or the auction price a better estimate of the value six months earlier; but such disagreements are rarely the stuff of clear error, and they are not here.

It may seem that the judge was, if anything, unduly generous to Proud, in giving Greycas only the value of the collateral on the date of default, rather than the unpaid principal of the loan. But for Proud's misrepresen-

tations, Greycas would not have made the loan, so its damages are not just the collateral but the entire uncollectable portion of the loan together with the interest that the money would have earned in an alternative use. Evidently, though, Greycas has been able to recover some of its principal out of other assets of Crawford's estate; for it originally asked the district court for the unpaid balance of the loan, and only later amended its complaint to ask just for the value of the collateral on the date of the default. Of course if Greycas had hopes of recovering out of the other assets of the estate more than the difference between the unpaid balance of the loan and the value of the collateral, there would be a serious question whether it had actually sustained the full damages that it is seeking in this action. It claims, however, that the other assets are worth less than this difference, and while Proud contests this claim, the district court did not commit clear error in taking Greycas's side in the dispute. We therefore conclude that the realizable value of Greycas's collateral on the date of Crawford's default was a real loss.

A final point. The record of this case reveals serious misconduct by an Illinois attorney. We are therefore sending a copy of this opinion to the Attorney Registration and Disciplinary Commission of the Supreme Court of Illinois for such disciplinary action as may be deemed appropriate in the circumstances.

AFFIRMED.

BAUER, *Chief Judge*, concurring. I am in agreement with the majority opinion. I believe that Proud would be liable without reference to legal malpractice or negligent misrepresentation. The evidence in this case indicates that he is guilty of fraud or intentional misrepresentation. He was lying when he represented that he had made U.C.C., tax and judgment searches on his brother-in-law's farm. He intended the misrepresentation to induce Greycas to make a loan to his brother-in-law; Greycas justifiably relied upon the misrepresentation in making the loan and was injured as a result. Under these facts, Proud's misrepresentation was indefensible.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

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United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

Before

Hon. WILLIAM J. BAUER, Chief Judge
Hon. WALTER J. CUMMINGS, Circuit Judge
Hon. RICHARD A. POSNER, Circuit Judge

GREYCAS, INC.,
Plaintiff-Appellee,

No. 86-2340 *v.*

THEODORE S. PROUD,
Defendant-Appellant.

Appeal from the United States District Court for the Southern District of Illinois, Alton Division.

No. 82 C 5138

William L. Beatty, Judge.

ORDER

On August 17, 1987, defendant-appellant filed a petition for rehearing. All of the judges on the original panel have voted to deny the petition. The petition is therefore DENIED.

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS

GREYCAS, INC., a corporation
Plaintiff,

vs.

THEODORE S. PROUD, JR., and PETER J. McGRATH, Individually, and as partners d/b/a McGrath and Proud,
Defendants.

No. 82 C 5138

ORDER

On May 28, 1986 the court entered herein its Findings of Fact and Conclusions of Law in the above-captioned matter. Thereafter, on June 5, 1986, defendant filed its "Motion to Amend Findings and Make Additional Findings Under Rule1 (sic) 52b". On June 12, 1986, plaintiff filed its "Motion to Correct Clerical Errors". Both of these motions were argued on June 26, 1986 and the court finds that there were indeed certain clerical errors or errors in addition that must be corrected.

IT IS THEREFORE ORDERED that the original "Findings of Fact and Conclusions of Law" entered on May 28, 1986 is hereby vacated and set aside and the following shall stand as the "Findings of Fact and Conclusions of Law".

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This action came on for trial and was tried on March 10-14, 1986, adjourned to and concluded on March 26, 1986, on the issues made by the pleadings, before the court sitting without a jury; and the parties appearing in person and through their respective attorneys, and the court having heard the testimony, examined the other evidence adduced by the respective parties, and heard the arguments of counsel, and being fully advised herein, makes the following findings of fact and conclusions of law:

FINDINGS OF FACT

1) At all times material hereto, Defendant Proud was an attorney at law licensed to practice in the State of Illinois.

2) Defendant Proud failed to exercise the standard of care of a reasonably prudent attorney and was negligent in the giving of his opinion letter of March 19, 1981, addressed to Plaintiff Lender, in which he stated:

> "I have conducted a U.C.C., tax, and judgment search with respect to the Company as of March 19, 1981, and except as hereinafter noted all units listed on the attached Exhibit A ("Equipment") are free and clear of all liens or encumbrances other than Lender's perfected security interest therein which was recorded March 19, 1981, at the Office of the Recorder of Deeds of Fayette County, Illinois. . ."

whereas, he did not conduct such search to determine that there were no prior liens or encumbrances or that Lender's perfected security interest was recorded on March 19, 1981, and no liens or encumbrances were found on the equipment listed on Exhibit "A" referred to in said opinion letter, other than plaintiff's perfected lien, but, instead, relied upon the assurances of the Borrower, Wayne Crawford, who engaged him, that "everything had been taken care of."

3) Defendant Proud knew that said opinion letter was

to be delivered to plaintiff, knew and expected that plaintiff would rely on said opinion letter and attached list of equipment in making the loan in question, and plaintiff did so rely thereon, the unrebutted testimony showing that plaintiff would not have made the loan if the opinion letter and list attached had not first been received by it.

4) A financing statement showing plaintiff as the Secured Party and the said Wayne Crawford as the Debtor was filed in the office of the Recorder of Deeds of Fayette County, Illinois on March 19, 1981; however, the list of equipment attached to said financing statement was not the same list that was attached as Exhibit "A" to the opinion letter of defendant, when delivered to the plaintiff, and covered none of the equipment (except above vehicular items) listed on said Exhibit "A" and perfected no security interest in plaintiff in the 3 items of vehicular equipment listed on the attachment to said financing statement.

5) The equipment in question and the rights of parties having a claim thereto, including plaintiff, were the subject matter of a cause of action in the Circuit Court of Fayette County, docketed in said court as Cause No. 82-Ch-11. As a result of the judgment entered in said cause, plaintiff lost the value of the collateral upon which it relied in making its loan, to the extent found herein.

6) Loss of the value of the collateral, the security of which plaintiff relied upon, to the extent found herein, was the proximate result of and was proximately caused by the negligent acts and conduct of defendant as (sic) aforesaid.

7) Defendant may have proved negligence upon the part of plainiff (sic) but that negligence, if any, had no causal relationship to the malpractice of defendant or the damages to the plaintiff.

8) A comparison of the items of equipment on Exhibit "A" attached to the opinion letter of defendant with those listed on Exhibit "B" attached to the Loan and Security Agreement shows that the sixty eight (68) items referred

to in the computation of damages hereinafter following, were listed on said Exhibit "A" and can be identified with and matched to the description of the same items on said Exhibit "B" when we consider all the evidence with reasonable inference.

9) The auction price received for the collateral equipment in September 1982 does not establish the value of the equipment at the time of default on March 1, 1982, because the auction sale took place under the worst circumstances, including the death of Crawford and the cloud of potential expensive litigation, and there was no evidence that equipment was maintained or kept sheltered during the interim period between default and sale, as it had been between the time of the loan and the time of default.

10) The evidence adduced on cross-examination of the Witness Evey, as to the telephonic evaluations of certain items of the collateral equipment, the appraisers contacted not having had the opportunity to visually inspect the equipment, is not considered as credible evidence of value.

11) The appraisal by the Witness Renner made on March 11, 1981, is a reasonable starting point to determine value, based upon his long experience as a dealer in farm machinery and the many appraisals of farm machinery made by him, and particularly because he personally inspected and viewed the condition of the equipment; that appraisal, when considered with Renner's testimony that used farm machinery depreciates at the rate of 15% annually, and plaintiff's own opinion testimony that the machinery here would depreciate at the rate of 20% annually, is the best evidence of the value of the collateral equipment at the time of default. The value of the equipment as of the date of default on March 1, 1982, is therefore fixed at the appraisal value of March 4, 1981, less 20%.

12) Based upon the foregoing, Plaintiff was deprived

of and lost the value of equipment (as listed on Court's Exhibit No. 1 attached hereto) which it otherwise would have had as collateral for its loan as follows:

APPRAISAL VALUE

	3/4/81	3/1/82) (less 20%)
68 items appearing on both Exhibits "A" and "B" disposed of by Judgment of Circuit Court of Fayette County	$ 1,042,200.00	$ 833,760.00

The aforesaid calculation does not include items against which Greycas still has a claim or upon which it has received any proceeds, the amount of which, when added to the damages found above, does not exceed the principal balance due on the note, nor the total value of all equipment on Exhibit "A" as of the time of default.

13) The principal balance due on the note for which the collateral would otherwise have been security was the amount of $1,167,769.24 at the time of default.

CONCLUSIONS OF LAW

1) The court has jurisdiction of the parties and the subject matter herein.

2) Plaintiff's reliance on the opinion letter and list of equipment attached hereto as Exhibit "A" could only extend to those items of equipment listed on said Exhibit "A" which were also listed on Exhibit "B", attached to the Loan and Security Agreement.

3) The effect of the judgment rendered in Cause No. 82-Ch-11 in the Circuit Court of Fayette County, Illinois, was to establish prior security interests in the collateral question in parties other than the plaintiff.

4) The burden of proving comparative negligence upon the part of plaintiff was on the defendant.

5) The release of lien purportedly executed by plaintiff and filed in Fayette County, Illinois was not executed by plaintiff and was a forgery.

6) The law is with the plaintiff and against the defendant and plaintiff is entitled to have judgment against defendant for the sum of $833,760.00, plus costs to the extent permitted by law.

DATED: This 15 day of July, 1986.

/s/ WILLIAM L. BEATTY

WILLIAM L. BEATTY
UNITED STATES DISTRICT JUDGE

AO 450 (Rev. 5/85) Judgment in a Civil Case

United States District Court

SOUTHERN DISTRICT OF ILLINOIS

GREYCAS, INC., a corporation

v.

THEODORE S. PROUD, JR., and PETER J. McGRATH, Individually, and as partners d/b/a McGrath and Proud

AMENDED
JUDGMENT IN A CIVIL CASE

CASE NUMBER: 82-5138

☐ **Jury Verdict.** This action came before the Court for a trial by jury. The issues have been tried and the jury has rendered its verdict.

☒ **Decision by Court.** This action came to trial or hearing before the Court. The issues have been tried or heard and a decision has been rendered.

IT IS ORDERED AND ADJUDGED that judgment is entered in favor of the Plaintiff, Greycas, Inc., a corporation, and against the Defendant, Theodore S. Proud, Jr. in the sum of $833,760.00, plus costs to the extent permitted by law. ----------

FILED
JUL 15 1986
A. MARVIN HELART
CLERK U.S. DISTRICT COURT
SOUTHERN DISTRICT OF ILLINOIS
ALTON OFFICE

July 15, 1986
DATE

A. MARVIN HELART
Clerk

/s/ PATRICIA A. BROWN
(By) Deputy Clerk

Supreme Court, U.S.
FILED
JAN 6 1988
JOSEPH F. SPANIOL, JR.
CLERK

No. 87-931

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

THEODORE S. PROUD, JR.,

Petitioner,

vs.

GREYCAS, INC., a corporation,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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ORAL ARGUMENT REQUESTED

SCHNEPP & BARNES-PRINTERS, INC., SPRINGFIELD, ILL.

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No. 87-931

IN THE

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OCTOBER TERM, 1987

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vs.

GREYCAS, INC., a corporation,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

STATEMENT OF FACTS

Petitioner's Statement of the Case is a lengthy dialogue dealing with the loan transaction and the parties involved. It contains inaccuracies and innuendo drawn from incomplete statements, all of which fade into insignificance when the case is placed in its proper perspective.

This was not a suit to recover the balance due on the loan. If it were, the lengthy recitation of facts by Petitioner might be pertinent. Rather, this was a suit to recover the value of collateral lost as a result of Respondent's reliance on the opinion letter of Petitioner.

The basic facts can be stated more simply. On March 11, 1981, Greycas, an Arizona company, entered into a Loan and Security Agreement with one Wayne D. Crawford, of Vandalia, Illinois, pursuant to which, Greycas agreed to loan Crawford the sum of $1,367,966.50. Collateral for the loan consisted of farm machinery and equipment comprising a three-page list, having an appraised value in excess of the loan amount. The Agreement provided that Crawford should deliver to Greycas a favorable opinion of his independent legal counsel in the form attached to the Agreement as an exhibit, assuring that title to the collateral was free and clear and that a perfected UCC-1 filing on behalf of Greycas was a first and prior lien.

(Much is made by Petitioner of the assertion that Respondent's Credit Committee ordered its own attorney to conduct the title search and that he unilaterally decided to rely on the title opinion of Petitioner. The Credit Committee merely documented by minute that the title search was a requirement of the loan and that it should be taken care of by the Legal Department. There was competent testimony in explanation of the minute and that the Legal Department did take care of it in accordance with its usual procedure, which was to have the borrower secure independent counsel for that purpose, as provided in the loan documents.)

Crawford engaged the services of Defendant Proud, an attorney who conducted his practice in Schaumburg, Illinois, to furnish the opinion letter. The opinion letter was on the stationery of Proud's firm, addressed to Greycas's parent company, dated March 19, 1981, and attached to it was the three-page list of farm equipment and machinery, the condition of title to which was the subject of the opinion letter. Proud testified that, in signing the opinion letter, he did so in reliance upon the statements and representations of Crawford, who was also an attorney, that everything had been taken care of, that a search had been made of the records, and that the UCC filing (on behalf of Greycas) had been made as shown by the letter.

Proud further testified that he knew that Crawford was obtaining a loan from Greycas and that Greycas would rely upon his opinion to the effect that title to the collateral was clear and that Greycas had a perfected security interest in the collateral.

Upon being furnished with the opinion letter of Proud, and verifying that he was a member in good standing of the Illinois Bar, and upon satisfaction of other provisions of the Loan and Security Agreement, Greycas made the loan to Crawford. When default occurred a year later, a number of state-court actions involving liens against Crawford's farm machinery and equipment were consolidated and tried before the Circuit Court of Fayette County, Illinois, which entered a Judgment determining the relative priority rights of the lien claimants. Greycas' claim to any of the items for which Judgment was entered in this case was extinguished by the Fayette County Judgment.

Crawford was the brother-in-law of Proud, a fact not disclosed to Greycas and of which it had no knowledge until default. It was clearly established at trial that Respondent had no cause of action against the borrower's wife since her name and that of the notary taking her acknowledgement were forged on the loan documents. Equally clear was the fact that she would retain her life insurance proceeds subject only to the claim of the Internal Revenue Service under transferee rules, that no part of the insurance proceeds would inure to the benefit of the estate or its creditors, and that there were no assets in the estate to satisfy the claims of creditors such as Greycas.

ARGUMENT

I.

The question of when a non-client may maintain suit against an attorney involves only state law.

Petitioner poses the question of whether the decision in *National Bank v. Ward*, 100 U.S. 195 (1878), which required privity of contract in order to maintain a suit against an attorney, is still a viable decision and whether it should be followed in the case at bar.

Whether *National Savings Bank v. Ward* is still a viable decision is immaterial to the resolution of this case since that decision merely interpreted the law of the District of Columbia as it existed over 100 years ago. That decision in no way created any federal rule. The fact that some states have elected to follow it while others, including Illinois, have elected otherwise, (*Pelham v. Greisheimer*, 91 Ill.2d 13, 440 N.E.2d 96 (1982)) does not furnish grounds for certiorari. Rule 17.1(a), Supreme Court Rules.

In any event, the facts of *National Savings Bank v. Ward* are distinguishable from this case. In *National Savings Bank v. Ward*, Mr. Chapman retained the services of Mr. Ward to ascertain whether Mr. Chapman had clear title to a certain piece of real estate. Mr. Ward had no knowledge that the title opinion was to be given to anyone else or to be used for any purpose other than for information to Mr. Chapman. The Court makes specific reference to this distinctive feature where it said:

> "*. . . and the case shows that the service was performed for a third person without any knowledge that the certificate was to be used to procure a loan from the injured party.*"

In contrast, Petitioner in this case knew from the outset that the purpose of his title opinion was to enable the borrower to secure a loan from Respondent and the title opinion was specif-

ically addressed to Respondent. Petitioner also knew that Respondent would be relying on his title opinion in making its decision of whether borrower should receive the requested loan.

Because the decision in *National Savings Bank v. Ward* was not based upon any United States' constitutional provision, or federal rule, this Court should decline to exercise its supervisory authority.

II.

The Court of Appeals did not depart from *Erie v. Tompkins.*

Petitioner's attempt to invoke the doctrine of *Erie RR Co. v. Tompkins*, 304 U.S. 64, is a circuitous effort to create a federal question where none exists. The injection of this doctrine where the underlying state law and facts of this particular case are not supportive of Petitioner's position is nothing more than an attempt to boot-strap Petitioner into the arena of federal law.

A. The duty is established by the court of last resort of the State of Illinois.

Petitioner states that the Seventh Circuit and the District Court disregarded what he claims to be the adversarial posture of the parties, which he contends negates the duty in this case. The opinion of the Seventh Circuit Court of Appeals belies this contention (Pet.App.4a). The Court there considered the argument that Greycas had an adversarial relationship with Proud's client, and that a lawyer has no duty of straight dealing to an adversary, and it was Proud's argument in his Brief in that Court that led to the dissertation by that Court on the question of negligent misrepresentation vis-a-vis professional malpractice.

But, to avoid the authority of *Pelham v. Greisheimer*, 92

Ill.2d 13, which establishes the duty, Petitioner quotes from that case (p. 23):

> "*In cases of an adversarial nature, in order to create a duty on the part of the attorney to one other than a client, there must be a clear indication that the representation by the attorney is intended to directly confer a benefit upon the third party.*",

and then argues that Respondent was, at most, an incidental beneficiary. The Seventh Circuit Court's opinion furnishes the complete answer to that argument at Pet.App.5a, where, after restating the proposition quoted from *Pelham*, it said:

> "*That, however, describes this case exactly. Crawford hired Proud not only for the primary purpose, but for the sole purpose, of influencing Greycas to make Crawford a loan.*" (Underscoring ours.)

The remaining Illinois cases cited by Petitioner enunciate different principles of law, or are clearly distinguishable on their facts. Suffice it to say that none holds that the parties to a loan transaction are in an adversarial position, nor does any contain a holding opposite to that of the Seventh Circuit in this case.

B. Respondent had a clear right to rely on Petitioner's opinion letter addressed to it.

Petitioner next argues that Respondent had no right to rely on Petitioner's opinion letter because (1) it had a duty to make inquiry as to the truth of the representations, and (2) UCC statements are public records and Respondent had equal access to the Recorder's office.

The cases cited by Petitioner in support of the first proposition have no application because they deal with fraudulent misrepresentation and not professional malpractice.

With respect to the second proposition, the case of *Chas. Hester Enterprises, Inc. v. Ill. Founders Ins. Co.*, 114 Ill.2d 278, simply held that state Statutes are matters of public record and

all persons are presumed to know their contents.[1] That is a far cry from the condition of a record title to be evidenced by a title opinion.

Again, the Seventh Circuit Court decided no federal question in conflict with a state court of last resort.

C. Petitioner's argument regarding damages is contrary to the evidence.

The points raised here are factually inaccurate and are answered in Respondent's Statement of the Case. Petitioner had no pending or viable action against the borrower's wife for the reasons shown by the evidence that her signature and that of her Notary on the loan documents were forgeries. Nor was a claim against the estate of the borrower of any value, for there were no assets in the estate to satisfy same, excepting as to two isolated pieces of farm equipment still in dispute, which were not included in the Court's assessment of damages. (Dist. Ct. Findings of Fact, Pet.App.22a.) Again, the argument about the availability to the estate of insurance proceeds is factually inaccurate. Clearly, the Findings of the District Court and the holding of the Court of Appeals on this element were not in conflict with any case of the Supreme Court of the State of Illinois.

III.

The prior state court Judgment.

It simply is not true that the prior state court Judgment was given preclusive effect. At no time during the trial of this case did Respondent ever assert the doctrine of res judicata or collateral estoppel with respect to the judgment of the Fayette County Circuit Court which determined the priority of the liens on the property in question. At no time did Respondent

---

1. In its holding to this effect, the *Hester* court was dealing with an issue of fraudulent concealment.

assert that such judgment was conclusive as to Petitioner or that he was precluded from contesting the issues or result of that case. And the Court so ruled during the trial. Nor did the Court, in its Findings and Conclusions, invoke the doctrine or rely on it. It merely stated that "The effect of the judgment . . . was to establish prior security interests in the collateral. . . ." (Pet.App.2a)

The Federal Full Faith and Credit statute, 28 U.S.C., Section 1738, reads in pertinent part:

> "*Such Acts, records and judicial proceedings or copies thereof, so authenticated, shall have the same full faith and credit in every court within the United States and its Territories and Possessions as they have by law or usage in the courts of such State, Territory or Possession from which they are taken.*"

In *Pile v. McBratney*, 15 Ill. 314, the Court said at p. 320:

> "*It is true, as a general rule, that a judgment or decree only binds parties and privies; and that, as against strangers, the record is only evidence of the fact that the judgment or decree has been pronounced, and of the legal consequences resulting from that fact.*" (Underscoring ours.)

The Court in *Illinois Steel Co. v. Indus. Com.*, 290 Ill. 594, affirms the proposition that a stranger may be affected by a judgment in a proceeding in rem. The Fayette County proceeding was unquestionably an in rem proceeding. It operated directly on the property affected. More importantly, Respondent submitted the Fayette County Judgment only to prove the legal consequences of its rendition. The Judgment was not offered to preclude Petitioner from relitigating any of the matters involved in that case, to do which he had full opportunity. The legal consequences of that judgment simply established *prima facie* or presumptively that Respondent did not have a first and prior lien on the collateral in question, as set forth in Defendant's opinion letter. No proof was offered in contravention, or to overcome this prima facie effect, nor did

the Seventh Circuit Court here decide a Federal question in conflict with a state court of last resort.

Moreover, and apart from the State Court Judgment, the Court admitted into evidence the records of the Recorder of Deeds of Fayette County, which showed that Respondent had no first and prior lien on March 19, 1981, covering the equipment put up as collateral, contrary to the statement of Petitioner in his opinion letter.

CONCLUSION

This was a diversity action in which the District Court and Seventh Circuit Court of Appeals followed and applied the substantive law of the State of Illinois. No federal question was presented, nor decided in a way in conflict with a state court of last resort. There is no call for an exercise of this Court's power of supervision.

Respectfully submitted,

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Supreme Court, U.S.
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No. 87-931

In The
Supreme Court of the United States
October Term, 1987

THEODORE S. PROUD, JR.,
Petitioner,

v.

GREYCAS, INC., a corporation,
Respondent.

PETITIONER'S REPLY BRIEF

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GREYCAS, INC., a corporation,
Respondent.

PETITIONER'S REPLY BRIEF

ARGUMENT

I.

RESPONDENT MAY NOT RECOVER WHERE IT WAS REPRESENTED BY ITS OWN ATTORNEYS.

Respondent erroneously states that the credit committee's direction that its own attorney should conduct the title search "merely documented" that a title search was a requirement of the loan (Brf. 2). Respondent further states that there was "competent testimony in explanation of the minute" and that it was "taken care of" by respondent's attorneys by leaving it up to the borrower's attorney (Brf. 2). The record shows otherwise. The direction by the Credit Committee to its own attorneys was as follows:

> A U.C.C. search must be conducted by the legal staff on used equipment.

Curt Brueckner, attorney for respondent, testified that he never asked his client what was meant by this directive, but that he understood this as a reference to the usual practice of having the borrower's attorney conduct the search. No member of the credit committee testified as to the meaning of this directive.[1] Irving Hymson, then Brueckner's supervisor and also responsible for this loan transaction, testified that on occasion the legal staff did conduct legal searches itself, contrary to its usual practice of relying on the other side. Respondent's assertion that the above directive was simply a documentation of the usual practice and procedure is not supported by this record.

Notably, the respondent has not attempted to rebut, either by reference to the record or to Illinois law, the uncontested fact that at all times the respondent was represented by its own attorneys. Instead, respondent seeks to avoid Illinois law on the element of "justifiable reliance" by stating that none of the cases cited to by petitioner involved professional malpractice (Brf. 6). In fact, there are three Illinois cases which hold that where a party is represented by counsel, any reliance on the other side's attorney is unjustified as a matter of law (Pet. 16-17). Two more cases discussed by petitioner, *Bloomer Amusement Co. v. Eskenazi*, 75 Ill.App.3d 117, 394 N.E.2d 16 (1979) and *Practical Offset, Inc. v. Davis*, 83 Ill.App.3d 566, 404 N.E.2d 516 (1980) hold that a party to a loan transaction may not rely on the other side's attorney to take the necessary steps to protect his own interests.

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[1] One member of the credit committee, Carole Sullivan, was asked this, but the objection to the question was sustained at trial when the evidence deposition was offered.

The respondent, like the district and appellate courts, ignores the vital fact that it was represented by its own attorneys. This fact, because this is a negligence action, defeats any duty owed by the petitioner to the respondent, eliminates any right the respondent had to rely, and bars any recovery, except against its own attorneys.

II.

RESPONDENT HAS A VIABLE ACTION AGAINST THE CO-SIGNER AND GUARANTOR OF THE LOAN.

Respondent also asserts it was "clearly established" that there was no cause of action against the co-signer, the borrower's wife, because her signature had been forged (Brf. 3,7). Petitioner respectfully disagrees. Although there was some evidence that her signature had been forged on the loan agreement, she also signed a personal guarantee for this loan. There was no evidence to show that the personal guarantee was not signed by her. The district court made no findings on the claimed forgery of the loan agreement.

The borrower's wife not only received $ 14,000 as a spouse's award in the probate court, but was also the beneficiary of two trusts, totalling $ 2.25 million from life insurance proceeds.[2] Thus, respondent has a viable cause of action against the guarantor of this loan, and has yet to sustain damages.

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[2] Petitioner agrees with respondent that the $4.0 million in insurance proceeds will not become part of the estate for the purpose of satisfying creditors' claims, after further review of the testimony. However, the guarantor was beneficiary of $2.25 million of these proceeds to be held in two trusts.

III.

THE ADMISSION AND PRECLUSIVE EFFECT GIVEN TO THE STATE COURT JUDGMENT VIOLATES 28 U.S.C. § 1738 AND THE DUE PROCESS CLAUSE.

Respondent does not challenge petitioner's analysis of the law as to the doctrine of collateral estoppel, but instead states that because it did not assert the doctrine by name, it somehow was not applied. It cannot be contested that the district court, in its findings, gave the prior state judgment preclusive effect.[3] Nor can it be contested that the Seventh Circuit held that a prior state court judgment is admissible in a federal court even though a state court would not have deemed it either admissible or binding on a non-party. Because the petitioner was not a party to the prior state action and had no opportunity to litigate the issues in the prior state suit, it is a violation of petitioner's due process rights to hold him conclusively bound to that judgment. *Kremer v. Chem. Const. Co.*, 456 U.S. 461, 481-83 (1982).

The claim that there is no federal question presented as to this issue (Brf. 7-8) is undercut by respondent's citation to 28 U.S.C. § 1738, not to mention the constitutional question of due process. Section 1738 operates to make the doctrines of *res judicata* and collateral estoppel applicable in federal courts when there has been a state court determination. *Kremer*, 456 U.S. at 481 n. 22. The effect of a prior court judgment is, however, subject to that state's law. *Kremer*, 456 U.S. at 481. Because in Illinois the doctrine of collateral estoppel would not apply, nor would the judgment be admissible, a federal question as to 28 U.S.C.

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[3] The judgment was the only document admitted into evidence to prove that there was a loss of collateral. Contrary to respondent's implication, not all records of the Recorder of Deeds were admitted into evidence, although the index was. What was not admitted was the other financing statements of other creditors, which would have been competent evidence.

§ 1738 and constitutional principles is raised.

Respondent cites to *Illinois Steel Co. v. Industrial Comm'n*, 290 Ill. 594, 125 N.E. 252 (1919) for the proposition that a stranger to that proceeding may be affected by a judgment in an in rem proceeding (Brf. 8).[4] The Illinois Supreme Court's holding was:

> A judgment may be offered in evidence against one who was neither party nor privy to the suit in which it was rendered for the purpose of establishing the fact of its own rendition and those legal consequences which would result from that fact, *but there is a material difference between proving the existence of a record and using the record to prove matters of fact found by it. A judgment cannot be introduced in evidence to establish the facts upon which it has been rendered except against parties to the suit or their representatives, because no one can be affected by proceedings to which he is a stranger* unless the judgment is upon some subject of a public nature, as in the case of inquisitions on behalf of the public, which are in the nature of proceedings in rem. (emphasis added).

Illinois Steel, 290 Ill. at 595-96, 125 N.E.2d at 253. The court then went on to hold that an order entered in probate court declaring a woman to be the deceased's wife was inadmissible in a proceeding before the Industrial Commission, which was to decide who was entitled to compensation under a workmen's compensation statute. *Illinois Steel*, 290 Ill. at 596, 125 N.E.2d at 254.

Without citation or explanation, respondent asserts that the state court proceeding was "unquestionably an in rem proceeding" (Brf. 8). It is impossible to determine from this broad statement what the respondent's position

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[4] The 135-year old case also cited by respondent is inapposite. In *Pile v. McBratney*, 15 Ill. 314, 319 (1853), the court held that jurisdiction may be obtained through notice by publication. Service through publication is not the issue in this case.

is as to case law involving *in rem* proceedings as applied to the issues presented in this case. *See, Shaffer v. Heitner*, 433 U.S. 186, 196-212 (1977). Assuming, *arguendo* there was any applicability, an assertion of jurisdiction still must meet constitutional mandates, and a court cannot assert jurisdiction and affect interested parties unless due process standards have been met. *Shaffer*, 433 U.S. 407, 409.

CONCLUSION

For the foregoing reasons, and those stated in the Petition, this Court should grant the Petition and give this matter its plenary consideration.

Respectfully submitted,

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